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February 1989 Monthly Survey

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Surveys of Consumers

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Consumer Sentiment Remains Favorable Despite Record Concerns With Rising Interest Rates

Index Remains At High Level

In the February 1989 survey, the Index of Consumer Sentiment was 95.4, down from 97.9 one month earlier, but above the 91.6 recorded one year earlier. Although the February Index receded from the 6 Index-point gain recorded in January, it still remained well above the December 1988 reading of 91.9. Overall, consumer confidence remained very favorable in the February 1989 survey, above the average level recorded during the current expansion.

The small February decline, like the more substantial January increase, was due to changing evaluations of buying conditions for large household durables. Despite the small decline, attitudes toward buying conditions remained favorable.

Among families with incomes of $40,000 or more the Index rose to 109.6 in February from 106.8 in January. The recent increase brought consumer confidence among high income families to its highest level since 1986.

Leading Indicator

The Index of Consumer Expectations, the expectations component of the Index of Consumer Sentiment and part of the composite Index of Leading Indicators, declined slightly to 88.8 in the February 1989 survey from 89.9 in January. It nonetheless remained substantially above the 85.5 recorded in December 1988 and the 80.1 recorded in February 1988.

The Index component reflecting assessments of current economic conditions declined to a larger extent, falling to 105.7 in February from 110.3 in January, and was slightly below the year earlier figure of 106.6.

Interest Rate Increases Expected by Record Numbers

Interest rates represent the top concern of consumers. The proportion of American families that expected increases in interest rates during the year ahead rose to 75 percent in the February 1989 survey, just above the 74 percent recorded in December 1988, and the highest level ever recorded in these surveys. Just 7 percent of all families expected declines in interest rates during the year ahead.

The increases in interest rates during the past year have come as no surprise to consumers. Following declines in interest rate expectations in the aftermath of the stock market crash in 1987,

interest rate expectations rose sharply in the first part of 1988. From February to June of 1988, the proportion of families that expected interest rate increases rose from 44 to 67 percent. Since then interest rate expectations have remained at very unfavorable levels.

As a result of the widespread concern over rising interest rates, consumers were more likely to favor borrowing in advance of the expected increases in interest rates rather than to view their current level as already too high and as a cause for postponement. Thus the recent increases in interest rates have had less of an impact on spending than might have been expected. Conversely, when consumers no longer expect further increases in interest rates, they will be more likely to then postpone purchases to take advantage of the expected future declines.

Inflation Expectations Ease

Consumers expected an annual rate of inflation of 4.8% during the year ahead in the February 1989 survey, down from 5.1% in January. The February reading was the lowest inflation rate expected since mid 1986 when inflation expectations were in the 5.5% range.

The February 1989 survey gave no evidence of a renewed building of inflationary psychology. Few consumers complained about drains on their purchasing power and few consumers favored purchasing in advance of rising prices. For the consumer, interest rate trends are a far more important consideration in their purchase timing decisions. Rather than viewing the expected^[increases in interest rates as the result of rising inflation, consumers were more likely to view the increases in interest rates as the reason inflation will be held in check.

Outlook for Economy Remains Favorable

Despite the heightened concerns with rising interest rates, consumers continued to view the outlook for the economy in relatively favorable terms, largely due to favorable employment prospects.

Although the majority of families expected the performance of the national economy to remain largely unchanged during the year ahead, the proportion that expected the economy to improve rose to 26 percent in the February 1989 survey from 23 percent in January and 19 percent in the December 1988 survey. Overall, good times financially in the country as a whole were expected by 56 percent of all families in the February 1989 survey, unchanged from January, and the highest level recorded during the past year.

The major factor underlying the maintenance of the favorable assessment of prospects for the national economy was the employment outlook. The majority of families in the February 1989 survey (55 percent) expected the current low rate of unemployment to remain largely unchanged during the year ahead.

Personal Finances Remain Strong

Consumers assessments of their own financial situation remained favorable in the February 1989 survey. Among all families, 44 percent reported that their financial situations had improved during the past year, unchanged from January, although slightly below the 47 percent recorded in February 1988. Increases in incomes were reported by 36 percent of all families in February, up from 34 percent in January. Reports of income declines, however, also increased, rising from 14 to 18 percent.

There is little evidence that the recent increases in inflation have influenced consumer evaluations of their financial situation. Complaints that rising prices had reduced living standards actually fell to 12 percent in February from 15 percent in January, and were only marginally above the 11 percent recorded in February 1988.

Consumers continued to view prospects for their own financial situation during the year ahead in favorable terms. Among all families in the February 1989 survey, 40 percent expected their financial situation to improve during the year ahead, just between the 41 percent recorded one month earlier and the 39 percent recorded one year earlier. Just 10 percent of all families expected their financial situation to worsen during the year ahead in the February 1989 survey. Income increases were expected by 66 percent of all families in the February 1989 survey, up from 60 percent one month earlier and 63 percent one year earlier.

Home Buying Conditions

Attitudes toward buying conditions for homes were unchanged in the February 1989 survey from one and two months earlier, but remain substantially below the levels recorded one and two years earlier. Among all families, 64 percent thought buying conditions for homes were favorable, down from 67 percent one year earlier and 81 percent two years earlier.

Rising mortgage interest rates have meant that fewer consumers now hold favorable views of the current level of mortgage rate. Thus far, however, the increases in mortgage rates have not been enough to make consumers choose to postponement purchases of homes. Indeed, since further increases in mortgage interest rates are expected, consumers are now more likely to cite the advantage of borrowing-in-advance of the expected increases in mortgage rates than favor the postponement of the purchase.

The proportion of families that mentioned the availability of low mortgage interest rates fell to 20 percent in the February 1989 survey from 44 percent one year earlier. Yet despite the recent rise in mortgage rates, the proportion of families that complained about high mortgage rates actually declined to 12 percent in February from 16 percent one month earlier and 15 percent one year earlier. Instead, more families referred to the advantage of borrowing-in-advance of rising interest rates--mentioned by 20 percent in the February 1989 survey up from just 6 percent one year earlier.

Car Buying Conditions

Favorable car buying attitudes were held by 61 percent of all families in the February 1989 survey, showing little change from prior surveys. For the past nine months the proportion of families holding favorable car buying attitudes has remained in the narrow range of 60 to 62 percent.

The recent round of price and interest rate discounts offered by vehicle manufacturers were reflected in the February data, but their impact was small. The proportion of families that mentioned the availability of price discounts rose to 30 percent in February from 28 percent in January. While references to the availability of discounted interest rates rose to 15 percent in February from 11 percent one month earlier.

Household Durables

The proportion of families holding favorable attitudes toward buying conditions for appliances, furniture, and home electronic goods retreated to 71 percent in the February 1989 survey from the 78 percent recorded in January. Overall, the February reading remained just between the 70 percent recorded in December 1988 and the 72 percent recorded in February 1988. When asked to explain their assessments, somewhat fewer consumers held favorable views of prices and interest rates on purchases of household durables.

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The February 1989 survey included 501 completed interviews conducted between February 1 and February 28, 1989.